



COUNCILMEMBER DONNA FRYE

CITY OF SAN DIEGO – SIXTH COUNCIL DISTRICT

Press Release

For Immediate Release
September 16, 2005

Contact: John Lamb
619-533-6460

COUNCILMEMBER FRYE PROTECTED RATEPAYERS AND FORCED SEWER DOCUMENT DISCLOSURES IN 2004

Provides Details on Exposing Culture of Secrecy

San Diego, CA -- Today, Councilmember Donna Frye detailed how in 2004 she protected sewer customers from paying more than their fair share, prevented the City of San Diego from being required to pay back early more than \$266 million in State grants and loans, and how she forced the release of documents to the Municipal Securities Rulemaking Board and the Nationally Recognized Municipal Securities Information Repositories (NRMSIRs).

"This is the perfect example of the culture of secrecy and business-as-usual that has existed at City Hall for years," Frye said. "I will continue working to make sure that the ratepayers and public interest are protected, and that more open government policies are adopted at City Hall."

Frye outlined a series of events beginning in January of 2002 that led to her exposing a cover-up of the city's sewer cost-of-service study. The documents show how Frye fought successfully to require the City to change its sewer rate structure to stop residential users from subsidizing the larger business users.

On May 14, 2002, Frye publicly questioned former Mayor Dick Murphy about the report at a City Council meeting and was told that it had never been discussed publicly -- despite the fact that minutes from an October 16, 2001, City Council meeting indicate otherwise.

Documents released by Frye also highlight a November 18, 2002, letter she sent to then City Attorney Casey Gwinn in which she objected to attending a closed session meeting where the cost-of-service study was docketed for discussion. In that same letter, she also filed a Public Records Act request to obtain documents that were being withheld from the public.

Frye provided a copy of a February 13, 2004, memo she sent to the City Manager that resulted in a March 26, 2004, Voluntary Disclosure statement by the city. Because of Frye's actions, the City Council voted in June 2004 to adopt rates that prevented residential customers from subsidizing larger users. The action also prevented the City from being required to pay back early more than \$266 million in State loans and grants and forced compliance with SEC regulations that require full disclosure.

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November 18, 2002

To: City Attorney Casey Gwinn
From: Councilmember Donna Frye
Re: November 19, 2002 Closed Session

Dear Casey,

I am writing to express my strong concerns about the legality of meeting in closed session on November 19, 2002 to discuss Item #7. In my opinion, this item does not meet the requirements of California Government Code section 54956.9(b)(1) regarding significant exposure to litigation, and should, therefore, be held in open session. While I rely upon the City Attorney for legal advice, it is the action of docketing #7 by your office that is causing me such concern and conflict.

I am also concerned about the circumstances under which this item was docketed and previously discussed in closed session, since the action did not involve pending litigation, anticipated litigation, or significant exposure to litigation. After researching the Brown Act requirements this weekend, I believe the action taken at that meeting was not authorized by some specific exemption and was done solely because it was considered controversial. Moreover, it is a direct result of the prior action in closed session that Item #7 has been docketed for the November 19, 2002 closed session.

I am requesting that you provide to me, in writing, a brief explanation and the specific sections of the Brown Act that:

- allow Item #7 to be docketed for closed session on November 19, 2002
- allowed the docketing of and past action taken in closed session (to withhold information from the public)
- provide necessary action to cure or correct the past action if it is determined that it was in violation of the Brown Act

I am also requesting that you provide me with a copy of the closed session docket for this item from earlier this year when it was first heard in closed session, the City Attorney memorandum that noticed the item and a copy of the existing study referenced in Item #7 per the Public Records Act.

I take my duties and obligations as a city councilmember very seriously and have been quite concerned about the issue discussed in Item #7 from the time it was first heard in closed session. The best I knew to do after the closed session, was to ask publicly that the study referenced in Item #7 be released. Despite the fact that it is a public document and its existence was common knowledge, when I asked about the study in open session I was told it did not exist.

Due to the urgency of this, I would appreciate your immediate attention and written response.

Thank you,

Honna Frye



COUNCILMEMBER DONNA FRYE

**City of San Diego
Sixth District**

MEMORANDUM

DATE: February 13, 2004

TO: Michael Uberuaga, City Manager

FROM: Councilmember Donna Frye *Donna Frye*

SUBJECT: Sewer Cost of Service Study disclosures in Sewer Revenue Bonds Preliminary Official Statement

Per my conversation today with Richard Mendes, Water Department Utilities General Manager, I am requesting confirmation that the Sewer Cost of Service Study disclosures will be included in the Sewer Revenue Bonds Preliminary Official Statement.

Thank you for your attention to this matter. Your timely response is greatly appreciated.

cc: Mayor Dick Murphy
City Council

DF/ks

San Diego officials reveal new omissions in financial reporting

By Philip J. LaVelle

The San Diego Union - Tribune. San Diego, Calif.: Apr 9, 2004. pg. A.1

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San Diego city officials have quietly disclosed more omissions in financial statements used by bond investors -- revealing, among other things, that the city is in danger of having to repay \$266 million in state and federal money for failing to restructure its sewer rates.

To avoid that, the City Council must impose a new rate structure on sewer users by July 1, according to state officials. A consulting firm has recommended increasing fees for commercial users of the city wastewater system and cutting fees for residential users, who according to the state bear a disproportionate share of the cost of sewer-system improvements.

Meanwhile, Moody's Investors Service yesterday placed the city on its "Watchlist," which signals that the city's creditworthiness is under review and that the city's credit rating could be lowered soon. Fitch Ratings and Standard & Poor's Ratings Services lowered the city's bond rating in February, citing previous admissions of errors and omissions in city financial statements. They also cited the city's troubled pension system, which has a \$1.1 billion deficit and more than \$1 billion in unfunded retiree health care costs.

A drop in its credit rating makes it more costly for the city to borrow money.

Also in February, officials confirmed that the FBI, the Securities and Exchange Commission and the U.S. Attorney's Office had begun an investigation into city finances. Independent experts suggest that investigators are looking for evidence of securities fraud.

The city's \$266 million exposure in the sewer matter -- never disclosed to the public and discussed by the City Council only behind closed doors -- was first relayed by the city to agencies that keep track of municipal debt on March 26.

At issue is the city's obligation, in exchange for receiving federal grants and low-interest state loans over the years, to rework sewer rates to make sure larger customers of the Metropolitan Wastewater Department pay their fair share for system improvements.

Upgrades include new pipes, pump stations and facilities designed to make treated wastewater dumped into the ocean less harmful to the environment.

The state Water Resources Control Board in November questioned whether the city was in compliance with the terms of the grants and loans. Last month, the board said the council must enact new rates by July 1.

Mayor Dick Murphy said he learned of the threat from the state only in the past month or so. He said he is optimistic that the City Council will meet the state deadline to revamp the fees.

"The reason that I believe that we'll be in compliance is because the alternative is so onerous," Murphy said.

The consulting firm of Black & Veatch of Overland Park, Kan., completed a report for the city that suggests slashing monthly bills for residential users by as much as 23 percent, according to Councilwoman Donna Frye, who said large retail-commercial users could see bills increase by up to 29 percent. Hospital sewer bills could go up as much as 5 percent; hotels could see up to 4 percent in hikes, Frye said.

Frye, a longtime clean-water activist, alleged that officials have intentionally dragged their feet while keeping the issue from public view.

"It's offensive to me," she said, "that our city doesn't feel the duty and the obligation to the public to disclose information that the public has a right to have."

Frye said the city has known since at least the late 1990s that it was not complying with state requirements for the grants and loans and has needlessly subjected residential users of the wastewater system to a heavier burden.

"People are paying a higher rate for their sewer services than they would if this system has been in place," she said.

Business interests are expected to lobby hard against possible sewer-rate increases, according to Eugene "Mitch" Mitchell, vice president of public policy at the San Diego Regional Chamber of Commerce.

"The bottom line is, businesses will realistically have to consider whether it is smart to continue operating in the city of San Diego . . . and if the (rate) changes are significant, it will definitely not be a welcome mat for businesses considering a move to San Diego," Mitchell said.

He cited other fee hikes, plus the council's 2002 vote to boost sewer rates 7.5 percent annually for four years. "This could turn us from a city of opportunity to a city of obstacles," Mitchell said.

The grants and loans to pay for sewer system improvements began heading the city's way in 1991, according to state officials.

In the March 26 document, city officials said the municipal bureaucracy has made several attempts over 16 years to get the City Council to adopt a new sewer-rate system. "However, none of those efforts ultimately proved successful," the report said.

The city's report to agencies that track municipal debt, issued by Deputy City Manager Patricia Frazier, added that the matter will be on the council's June 8 docket and that "city staff believes" the council will meet the state deadline.

But, pointing to past failures, the report warned that "... no assurances can be given that the City Council will approve the proposed user charge system."

The report said that "if at any time" the state water agency is dissatisfied with the city's progress, it has the power to require the city to "repay at least \$266 million."

Murphy said city officials are obligated to "paint the worst- case scenario." Asked why the city had not acted earlier, he said: "I'm not sure I have a good answer for that."

The mayor also said he did not recall discussing with Frye the timing of the sewer study. Frye said city officials, including Murphy, have known of the situation for a long time. She said the issue made the agenda of a City Council closed-session hearing on Nov. 14, 2002. The matter was not discussed, she said, because she raised issues about it being heard in secret.

"It was very clearly presented (in briefing documents) what the impacts would be if we did not comply with the conditions," she said.

The disclosure of the sewer system issue came in a broader report warning investors that the city would not release its financial report for the fiscal year ending June 30, 2002, until June of this year. City officials say the financial statement -- typically published in December -- is delayed because the financial-services firm KPMG is auditing city finances.

Moody's cited that delay as one of several reasons it placed San Diego on its Watchlist yesterday. It also warned of "heightened uncertainty regarding the city's financial position as it ended the last fiscal year, its (decision) to defer addressing its structural imbalance in the current fiscal year, and the daunting challenges it faces doing so in fiscal 2005."

In a written statement, Murphy said:

"In light of the previous actions by Fitch as well as S&P, I am not surprised that Moody's has put San Diego on its 'Watchlist.' I am hopeful that the city's responses to past auditing errors, the unfunded liabilities in its pension plan, and the Fiscal Year '05 budget challenges, will forestall a credit downgrade."

Moody's also raised concerns about turnover in key management positions -- the city auditor took early retirement last year and the city manager announced his resignation last month -- as well as an uncertain political climate.

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CHANNEL 10 REPORT --

Failing To Restructure Sewer Rates May Cost City \$266M

Frye Said City Withheld Public Information

POSTED: 3:53 pm PDT April 9, 2004
UPDATED: 5:10 pm PDT April 9, 2004

SAN DIEGO -- San Diego city officials disclosed more omissions in financial statements, meaning the city may have to repay \$266 million and lose the ability to receive federal and state grants for failing to restructure sewer rates, 10News reported.

To avoid that, the City Council must impose a new rate structure on sewer users by July 1, state officials said.

But, one City Council member said the omissions were part of a known "cover up" -- a cover up that could lead to federal securities violations.

At issue is the city's obligation to rework sewer rates to make sure larger customers of the Metropolitan Wastewater Department pay their fair share of system improvements.

The city's \$266 million exposure in the sewer matter -- never disclosed to the public and discussed by the City Council only behind closed doors -- was first relayed to the city on March 26 by agencies that keep track of municipal debt.

According to the released studies, the average San Diego household overpays their sewer rates by more than 23 percent, or \$11 a month.

District Six City Councilmember Donna Frye said there is a long paper trail of proof dating back to 1991 that the city was not in compliance with sewer rate fees when it accepted at least \$266 million in federal and state grants for large wastewater projects.

"These types of documents need to be released in a public forum at a City Council meeting," Frye, (pictured, right), said.

If San Diego's "approved user rate charge system" had been implemented, it would have lowered the average household sewer bill by \$11 per month, or more than a 23 percent. It would have also cost small retail businesses an extra \$55 per month or almost 16 percent more, according to 10News.

Those rate fees are important, because the city is required to use a fair rate system to receive the state and federal grant money.

In May 2002, Frye questioned Mayor Dick Murphy about the "sewer rate study."

"I was wondering when it might be released to the public," Frye told 10News.

But, Frye said the mayor orchestrated a cover up and won an 8-to-1 vote in a closed session to cover up the study.

"There was a vote on this to withhold documents (from the public)," Frye said.

Frye added the results were withheld from the public until the city was "absolutely forced to" show them.

According to city records, the meeting was closed to the public because it included possible litigation.

Last month, Frye completed an open-records request with the City Attorney's Office demanding the report. Within days, the city revealed in bond disclosure forms it could have to repay \$266 million for failing to meet the sewer rate fee requirements.

A legal expert said that if the forms are true, and what Frye said is accurate, the city could be violating federal laws.

Jim Krause, a bondholder's attorney, said, "(The city is) required by law to make sure the perspectives are complete. That's the first area of concern, whether the Securities Exchange Commission will find to see if there's a securities violation."

Krause, said if the value of municipal bonds already out there is downgraded based on a knowing non-disclosure, bondholders could sue in a class-action suit.

In addition to repaying the \$266 million, the city may also lose its ability to get new federal and state grant money.

Moody's Investors Service Thursday placed the city on its "Watchlist," which signals that the city's creditworthiness is under review and the credit rating could be lowered soon.

Mayor Dick Murphy said he believes the City Council will meet the state deadline to revamp the fees.

The consulting firm of Black & Veatch of Overland Park, Kan., recommended increasing fees for commercial users of the city waterway system and cutting fees for residential users, who bear a disproportionate share of the cost of sewer system improvements, state officials said. The consulting firm completed a report for the city that suggests slashing monthly bills for residential users by 23 percent. Large retail-commercial users could see bills increase by 29 percent, hospitals could see a 5 percent hike and hotels could see a 4 percent hike.

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